

Report of the auditor-general to Limpopo provincial legislature and council on Polokwane Local Municipality

Report on the audit of the consolidated and separate financial statements

Qualified opinion

1. I have audited the consolidated and separate financial statements of the Polokwane Local Municipality and its municipal entity set out on pages x to x, which comprise the consolidated and separate statement of financial position as at 30 June 2017, the consolidated and separate statement of financial performance, statement of changes in net assets, and cash flow statement and the statement of comparison of budget with actual amount for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matter described in the basis for qualified opinion section of my report the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of the group as at 30 June 2017, and their financial performance and cash flows for the year then ended in accordance with the applicable financial reporting framework and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA).

Basis for qualified opinion

Property, plant and equipment

3. I was unable to obtain sufficient appropriate audit evidence for the assessment of impairment at infrastructure assets for which indicators of impairment were identified as required by GRAP 21, *Impairment of non-cash generating assets* as I could not be provided with adequate supporting evidence. I was unable to confirm the assessment of impairment of the infrastructure assets by alternative means. Consequently, I was unable to determine whether any adjustment relating to infrastructure assets stated at R10 865 079 100 in note 8.1 to the financial statements was necessary.
4. I was unable to obtain sufficient appropriate audit evidence for the devaluation of land of R188 881 393 as the municipality could not substantiate the nominal rate used. I was unable to confirm the valuation of land by alternative means. Consequently, I was unable to determine whether any adjustment relating to land stated at R48 598 948 in the financial statements was necessary.
5. I identified a difference of approximately R159 400 156 between depreciation on note 8.1 and my recalculated amount as the municipality depreciated its assets using original cost of the asset over the useful life instead of using the re-valued carrying amount over the remaining life as required by GRAP 17: *Property, plant and equipment*. Additionally, there was a consequential impact on property, plant and equipment and the revaluation reserve. Consequently, there was an overstatement of property, plant and equipment and depreciation stated at R13 360 354 162 and R754 377 167 respectively in note 8.1 and revaluation reserve stated at R7 275 566 946 in the financial statements.

A handwritten signature in black ink, appearing to read 'J. S. M. 2018'.

Revenue from exchange transactions

6. I was unable to obtain sufficient appropriate audit evidence for the basis of estimations used on the consumption of water and electricity as the underlying records could not distinguish actual readings from estimated consumption. I was unable to confirm the accuracy of service charges by alternative means. Additionally, there was a consequential impact on trade and other receivables from exchange transactions. Consequently, I was unable to determine whether any adjustment relating to service charges stated at R1 183 014 132 in note 17 and trade and other receivables stated at R451 657 057 in the financial statements was necessary.

Expenditure

7. The municipality incurred expenditure of approximately R35 218 225 for payments that were already made. The municipality does not have an adequate system of internal control in place to detect duplicate payments. Consequently, there was an overstatement of general expenditure stated at R434 276 519 in the financial statements. Additionally there was a resultant impact on cash and cash equivalents.
8. I identified that the municipality did not capitalise expenditure of capital in nature but incorrectly expensed the cost as repairs and maintenance. The municipality does not have an adequate system of internal control in place to identify capital expenditure. Consequently, infrastructure assets stated at R10 865 079 100 was understated and repairs and maintenance stated at R258 470 751 was overstated by approximately R147 475 205.

Revaluation surplus

9. The municipality did not realise revaluation surplus included in nets asset in respect of items of property, plant and equipment as the assets are utilised in line with their accounting policy and GRAP 17: *Property, plant and Equipment*. I was unable to confirm the accuracy of revaluation surplus by alternative means. Consequently, I was unable to determine whether any adjustment relating to revaluation surplus stated at R7 275 566 946 in the financial statements was necessary.

Cash flow statement

10. The municipality included unexplained non-cash item amounting to R 73 434 676 in the reconciliation of cash generated from operations in note 31 to the financial statement. Consequently, I was unable to determine whether any adjustment was necessary to cash flow from operating activities stated at R843 159 972 in the financial statements.

Context for the opinion

11. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
12. I am independent of the group in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

A handwritten signature in black ink, appearing to read 'H C'.

13. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of matter

14. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Restatement of corresponding figures

15. As disclosed in note 30 to the consolidated financial statements, the corresponding figures for 30 June 2016 have been restated as a result of an error discovered in the financial statements of the municipality and the municipal entity at, and for the year ended 30 June 2017.

Significant uncertainties

16. With reference to note 34 of the consolidated financial statements, the entity is currently involved in litigation with various service providers, employees and third parties. The ultimate outcome of the matters cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

Material impairment

17. As disclosed in note 12 to the consolidated financial statements, material impairment to the amount of R562 061 708 (2016: R589 150 558) was raised to provide for irrecoverable trade debtors as a result of doubt over the collectability of the long outstanding consumer debts.

Irregular expenditure

18. As disclosed in note 35.3 of the consolidated financial statements, the municipality and the municipal entity incurred irregular expenditure of R198 919 195 (2016: R274 710 941) in contravention of the Municipal Supply Chain Management Regulations (MSCMR).

Other matters

19. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosures

20. In terms of section 125(2)(e) of the MFMA, the group is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Unaudited supplementary schedules

21. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.



A handwritten signature in black ink, appearing to read 'WJG', is located in the bottom right corner of the page. Below the signature is the number '3'.

Responsibilities of the accounting officer for the financial statements

22. The accounting officer is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with applicable financial reporting framework and the requirements of the MFMA and for such internal control as the accounting officer determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatements, whether due to fraud or error.
23. In preparing the consolidated financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting there is an intention either to liquidate the municipality or to cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

24. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.
25. A further description of my responsibilities for the audit of the consolidated financial statements is included in the annexure to the auditor's report.

Report on the audit of the annual performance report

Introduction and scope

26. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected key performance areas presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
27. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
28. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected key performance areas presented in the annual performance report of the municipality for the year ended 30 June 2017:

4

KPA	Pages in the annual performance report
KPA 2: Basic service delivery	64-69
KPA 5: Local economic development	26-40

29. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

30. The material findings in respect of the usefulness and reliability of the selected key performance areas are as follows:

KPA 2: Basic service delivery

Indicator 16: # of Environmental Educational Awareness Programme conducted by 30/06/2017

31. The reported achievement for target of 4 was misstated as the evidence provided indicated 5 programmes and not 4 programmes as reported

KPA 5: Local economic development

Indicator 1: Number of Job opportunities created through the municipal LED initiatives by 30/06/2017

32. The reported achievement for 170 targeted job opportunities created through municipal initiative was misstated as the evidence provided indicated 578 not 656 as reported.

Indicator 3: Number of job opportunities created through the EPWP by 30 June 2017

33. The reported achievement for 2 632 targeted job opportunities created through EPWP was misstated as the evidence provided indicated 3495 and not 2830 as reported.

Indicator 5: % Implementation IRPTS (Construction Phase) required to Go-Live targets.

34. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of target of 57%. This was due to limitations placed on the scope of my work as evidence could not be provided to support additional kilometre required to go-live and stage of completion for the control centre. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 57%.

Indicator 6: Number of SMME incubated

35. The reported achievement for target 54 was misstated as the evidence provided indicated 18 and not 158 as reported.

Indicator 7: Number of SMME capacitated (offering training, facilitate training, the municipality facilitates training, access to markets and linkage to financial institutions) support reported

36. Achievement for target 90 was misstated as the evidence provided indicated 490 and not 584 as reported.

Indicator 8: Number of SMME linked with market by 30 June 2017


5

37. The reported achievement for target 100 was misstated as the evidence provided indicated 349 and not 227 as reported.

Other matter

38. I draw attention to the matter below.

Achievement of planned targets

39. Refer to the annual performance report on pages x to x; x to x for information on the achievement of planned targets for the year and explanations provided for the under and overachievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs x; x; x of this report.

Report on audit of compliance with legislation

Introduction and scope

40. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

41. The material findings on compliance with specific matters in key legislations are as follows:

Annual report and annual financial statements

42. The consolidated financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of revenue and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and/ or supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Budget Management

43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R292 486 646, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by under budgeting on non-cash items.

Expenditure Management

44. Effective steps were not taken to prevent irregular expenditure amounting to R198 919 195 as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with SCM regulations and prescripts.

45. An effective system of expenditure control, including procedures for the authorisation and payment of funds, was not in place as required by section 65(2)(a) of the MFMA.

A handwritten signature in black ink, appearing to read 'H. J. G.' or a similar variation, is located in the bottom right corner of the page.

Procurement and Contract management

46. Awards were made to providers whose directors or principal shareholders are in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44.
47. Awards were made to providers whose directors or principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process as required by SCM regulation 38(1).

Conditional grant

48. The municipality did not evaluate its performance in respect of programmes or functions funded by the Public Transport Network Grant, Regional bulk infrastructure Grant, Neighbourhood development Grant and Municipal Infrastructure Grant as required by section 12(5) of the DoRA.

Information technology management

49. The information technology (IT) audit revealed significant control weakness due to key risks that were not adequately managed and mitigated within the IT areas, resulting in non-compliances with section 62(1)(c)(i) of the MFMA.

Other information

50. The municipality's accounting officer is responsible for the other information. The other information comprises the information included in the annual report, which includes the audit committee's report. The other information does not include the financial statements, the auditor's report thereon and those selected key performance areas presented in the annual performance report that have been specifically reported on in the auditor's report.
51. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
52. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed on the other information obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact.

Internal control deficiencies

53. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified, the findings on the annual performance report and the findings on compliance with legislation included in this report.
54. The municipality has an approved code of conduct, however this is not adequately utilised to create ethics in the work place and a sense of pride and responsibility for protecting and



safeguarding of municipal assets, as a result some officials have embarked on questionable conduct causing the municipality to suffer financial losses.

55. The municipality developed a plan to address internal and external audit findings, but the accounting officer did not adequately monitor adherence to the plan in a timely manner.
56. Corrective action actions have not been implemented to address the weaknesses in the information technology control environment identified by our audit process.
57. Leadership was slow in addressing weaknesses in the preparation of financial statements, management and reporting on performance information and monitoring of non-compliance with legislation non-compliance with legislation by the accounting officer, which resulted in a number of instances of noncompliance.
58. The municipality did not have a proper record management system to maintain information that supported the reported performance in the annual performance report. This included information that related to the collection, collation, verification, storing and reporting of actual performance information, as a result, the some of the key events affecting the financial statements and reported performance information were not adequately supported, resulting in the modification of audit financial statements and findings on performance information.
59. Weaknesses in the processes and controls over revenue management were not adequately addressed and the lack of regular monitoring and reconciliations of revenue information resulted in revenue information not being reliable.
60. Management has placed reliance on consultants for management and maintenance of the fixed asset register without proper monitoring of the activities of the consultants in the preparation and maintenance of the fixed asset register, as a result management was unable to properly account for and support the decisions taken by the consultants in accounting for assets.
61. The leadership did not effectively utilise the reviews of internal audit and audit committee to improve the quality of financial statements as the financial statements were submitted late to these structures and their reviews not adequately addressed due to time pressures.

Auditor-General

Polokwane

12 January 2018



A U D I T O R - G E N E R A L
S O U T H A F R I C A

Auditing to build public confidence

Annexure – Auditor-general’s responsibility for the audit

62. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the consolidated and separate financial statements, and the procedures performed on reported performance information for selected key performance areas and on the municipality’s compliance with respect to the selected subject matters.

Financial statements

63. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in the auditor’s report, I also:

- identify and assess the risks of material misstatement of the consolidated and separate financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control.
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
- conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the consolidated and separate financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the group’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause the group to cease operating as a going concern.
- evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

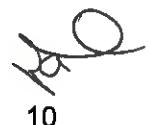
64. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

65. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and where applicable, related safeguards.



9

66. From the matters communicated to those charged with governance, I determine those matters that were of the most significance in the audit of the financial statements of the current period and are therefore key audit matters. I describe these matters in my auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, I determine that a matter should not be communicated in my report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest of such communication.

A handwritten signature in black ink, appearing to read "H. O." or a similar initials.